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No. 243

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In the Supreme Court of the United States

OCTOBER TERM, 1968

CITIZEN PUBLISHING COMPANY,
STAR PUBLISHING COMPANY,
TUCSON NEWSPAPERS INCORPORATED,
ARDEN PUBLISHING COMPANY AND WILLIAM A. SMALL, JR.,
Appellants,

v.

UNITED STATES OF AMERICA,
Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF ARIZONA

STATEMENT OPPOSING MOTION TO AFFIRM

RICHARD J. MACLAURY
THOMAS J. KLITGAARD
225 Bush Street
San Francisco, California 94104
Attorneys for Appellants

Of Counsel

JOHN L. DONAHUE, JR.
ROBERTSON & FICKETT
Tucson Federal Savings Tower
Tucson, Arizona 85702

GEORGE READ CARLOCK
RYLEY, CARLOCK & RALSTON
Title & Trust Building
Phoenix, Arizona 85003

PILLSBURY, MADISON & SUTRO
225 Bush Street
San Francisco, California 94104

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This is a response to the motion to affirm.

A. The Per Se Argument.

The government fails to meet the basic question presented in the jurisdictional statement. That question is whether the District Court erred in holding that the operating agreement was per se illegal "when the application of the rule

of reason would have resulted in sustaining the agreement" (J.S. 3.)*.

Instead, it evades the issue by assuming at the outset that the agreement is a per se violation. The government then goes on to argue a question that is not presented here, i.e., whether per se violations can be justified by business necessity (M. 12, 23). Phrasing the issue this way begs the question and assumes the answer. The issue is not whether per se violations can be justified. The issue is whether the agreement constitutes an unreasonable restraint, per se or otherwise.

The government attempts to twist this issue by misstating our position. It says that appellants apparently do not challenge the Court's conclusion that the joint operating agreement "provides for price fixing, profit pooling, and market allocations" (M. 12). To the contrary, we objected to that conclusion at the outset and have vigorously contested it ever since (J.S. 5, 6).†

The government is also mistaken when it asserts that appellants do not claim they were prejudiced in the defense of the operating agreement by the exclusion of material evidence (M. 17). One of the principal arguments in our jurisdictional statement was that the District Court decided

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*As used herein, "J.S." refers to the jurisdictional statement, "M." to the motion to affirm. "F." refers to the trial court's findings of fact, "C.L." to the trial court's conclusions of law, "Tr." to the trial transcript, "G.X." to the government's exhibits, and "D.X." to the appellants' exhibits.

†The government also contends that in our jurisdictional statement we do not challenge the District Court's conclusion that the provision not to engage in another publishing business in Pima County or any other business in conflict with the agreement constitutes "market allocation" (M. 14, fn. 10). The government is mistaken. We presented the question whether the operating agreement constitutes a violation of Section 1 of the Sherman Act (J.S. 3), and the "market allocation" issue is clearly a "subsidiary question fairly comprised therein" (Sup. Ct. Rule 15(1)(c)).

the Section 1 issue on summary judgment (J.S. 5). The ruling was based on the terms of the agreement (M. 9). As we have pointed out, the Court denied appellants' motion at the close of trial to set aside its summary judgment and reconsider the Section 1 issue under the rule of reason and in the light of the evidence adduced on the other issues in the case (J. S. 6). Further, as the government concedes, the entire Section 1 issue was excluded from the trial and "only the question of relief remained to be decided" (M. 9). The District Court denied appellants' discovery and rejected all offers of proof on the Section 1 issue. It was primarily the prejudice arising from these rulings and the denial of an opportunity to defend the Section 1 issue that brings appellants to this Court.

The prejudicial ruling on summary judgment was premised on the contention of the government that the agreement is a per se violation. This contention, made below and repeated in the motion to affirm, has no foundation. The government agrees that pursuant to the operating agreement "[t]he production and distribution equipment of each newspaper was placed in joint ownership, and possession of these assets was transferred to TNI" (M. 5), that TNI was "owned in equal shares by the Star and the Citizen, whose function would be 'to manage and operate all of the departments of the publishing business of Star and Citizen (excluding the news and editorial departments * * *), and to integrate the operation of said business as much as possible'" (M. 4). Thus, there was a mutual acquisition of assets owned by two separate firms, a termination of their former commercial businesses and a restructuring of their assets under new management. The result was the formation of a new business entity (TNI) which integrated and operated the acquired assets, priced its products and services and distributed revenues in excess of costs to its

stockholders. In every practical sense of the word, the transaction was a merger.*

The government acknowledges that it is "inappropriate to apply a *per se* rule to mergers" (M. 22). Clearly, therefore, the operating agreement must be judged under the rule of reason and in light of the facts peculiar to the business, to the market and to the purposes sought to be attained.†

The per se cases cited in the motion to affirm (M. 14, fns. 9, 10; M. 15, fn. 11) all involved agreements which were naked restraints of trade by viable competitors perfectly capable of operating their businesses independently.‡ *Northern Pac. R. Co. v. United States* (1958) 356 U.S. 1, 5, cited by the government, referred to these restraints as "agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are

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*See Kaysen and Turner, *Antitrust Policy* (Harvard University Press, Cambridge, 1965), p. 136, where it is said "joint purchase of existing assets * * * analytically differs little from the merger question." See also Zimmerman, *Adventures in Jointness*, 37 Antitrust Law Journal (1968) 125, 126, who states "the joint venture which involves a total and permanent combination of all or part of one company's resources with another is simply a merger."

†Cf. *United States v. Penn-Olin Co.* (1964) 378 U.S. 158, 161, 170, where this Court held that the joint venture agreement and concurrent acquisition of assets did not by themselves violate Section 1 of the Sherman Act.

‡*United States v. Trenton Potteries* (1927) 273 U.S. 392; *U.S. v. Socony-Vacuum Oil Co.* (1940) 310 U.S. 150; *United States v. Line Material Co.* (1948) 333 U.S. 287; *Kiefer-Stewart Co. v. Seagram & Sons* (1951) 340 U.S. 211; *Northern Pac. R. Co. v. United States* (1958) 356 U.S. 1; *United States v. General Motors* (1966) 384 U.S. 127; *United States v. Sealy, Inc.* (1967) 388 U.S. 350; *United States v. Addyston Pipe & Steel Co.* (6 Cir. 1898) 85 Fed. 271, affirmed 175 U.S. 211; *United States v. Aluminum Co. of America* (2 Cir. 1945) 148 F.2d 416; *Timken Co. v. United States* (1951) 341 U.S. 593; *United States v. Paramount Pictures* (1948) 334 U.S. 131; *Northern Securities Co. v. United States* (1904) 193 U.S. 197.

conclusively presumed to be unreasonable * * *." The government's authorities are not applicable to the situation here where a successful newspaper entered into an agreement with its failing competitor with the intent and effect of preserving a part of the failing company and providing the community with two rival sources of news.

Thus, the District Court's conclusion that the operating agreement constitutes "price fixing, profit pooling, and market allocation" is unsupported. After the merger and integration by TNI of the former business of Star Publishing and Citizen Publishing, the establishment by TNI of advertising and circulation rates cannot constitute "price fixing." If it did, every horizontal merger or joint venture would be illegal per se. For the same reason, the distribution of revenues by TNI to its stockholders cannot be illegal "profit pooling." A merger or joint venture does not become unlawful simply because its revenues are distributed among the owners. And the provision against engaging in conflicting businesses is not "allocation of markets." The provision merely expresses the obligation implied by law that participants in a common enterprise must act in good faith and may not cripple or injure the enterprise. (See *Tovrea Land and Cattle Company v. Linsenmeyer* (1966) 100 Ariz. 107, 412 P.2d 47, 57; *Red Top Cab Co. v. Hanchett* (N.D. Calif. 1931) 48 F.2d 236, 238).

B. The Failing Company Doctrine.

The government argues that the "failing company" doctrine does not apply here because "essential elements of that defense did not exist" in 1940 (M. 18). First, the government contends there is substantial evidence to support the District Court's conclusion (F. 17) that when the operating agreement became effective Citizen Publishing was

not on the verge of going out of business (M. 13). We have shown that there is no such evidence (J.S. 12). Further, this conclusion by the District Court contradicts its prior findings that from 1932 to 1940, Citizen Publishing operated at a substantial loss (F. 12), that from 1937 to 1940, Citizen Publishing lost money (F.14), that between 1937 and 1939, Small, Sr., made unsuccessful efforts to attract additional financing (F. 14), that for many years prior to 1940, Citizen Publishing had been unable to pay a dividend (F. 15), that prior to 1940, Small, Sr., received no salary (F. 15), and that by March, 1940, Citizen Publishing owed debts of more than $109,000 (F. 15). These contradictions demonstrate that a mistake has been committed by the District Court. (See *United States v. Gypsum Co.* (1948) 333 U.S. 364, 394-395.) Clearly the conclusion in Finding 17 is erroneous.

Second, the government attempts to deprecate the efforts of Small, Sr., to attract additional financing by saying that he merely "sought to interest three of his personal acquaintances in investing some money in the Citizen, but they were not prepared to do so at that time" (M. 19). The record shows that Small, Sr., did the best he could to refinance Citizen Publishing by soliciting persons interested in newspapers and experienced in the communications business (F. 15, Tr. 798-799). It is understandable that these people declined, because at that time the newspaper business throughout Arizona was a decidedly poor investment risk.*

Responding to the argument that Small made no effort to sell his newspaper to an outside party, we point out that the evidence is undisputed that it was impossible to have

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*During the ten-year period, 1930-1940, the Phoenix *Arizona State Democrat* (1931) and the Phoenix *Bee Messenger* (1932) suspended publication entirely; the Globe *Record* (1931) and Winslow *Mail* (1932) changed from dailies to weeklies (American Newspaper Publishers Association Bulletin No. 5203, July 27, 1950).

sold Citizen Publishing in 1940 to an outside publisher who had any expectation of operating the newspaper at a profit (Tr. 840).

In the absence of evidence that Citizen Publishing could long survive, the government argues that the newspaper was not in danger of failing, because, otherwise, "it is difficult to explain" why the owners of Star were willing to share its imminent monopoly profits with a competitor headed for extinction (M. 20). This speculation is contradicted by the record. Mr. Mathews, the publisher and one of the owners of Star, testified that he knew for a fact that Citizen was not operating at a profit and that "it would eventually have to give up the ghost" (Tr. 764). He explained that he had refused numerous offers from persons other than Small, Sr., to merge Citizen Publishing with Star Publishing (Tr. 765-768). He also explained that he eventually entered the operating agreement because he thought Tucson should have separate news and editorial voices, even though it could not support two entirely separate newspapers.*

The government also argues that the failing company doctrine is not a defense because Citizen Publishing could have taken steps short of the operating agreement to solve its financial problems (M. 21). It contends that the parties should have resorted to joint printing and joint distribution alone and that this would have enabled Citizen Publishing

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*"I didn't want to see a monopoly in Tucson; I didn't want to be connected with a monopoly in Tucson or anywhere else. But I saw that this plan of unification of the business side of the paper would preserve two independent voices in Tucson. To me that is the important consideration and I say that if this hadn't worked out eventually I would have been offered the Citizen, they had to offer it to me eventually, and then I would have been a monopolist here in Tucson with only my voice being heard and no other voice being heard.

* * *

"That was a situation I wanted to avoid." (Tr. 777).

to survive (M. 12, 20-21). The uncontradicted evidence showed that the 1940 consolidation of the printing and distribution facilities yielded average annual savings for Citizen Publishing over the next three years of less than $9,000 (D.X. 176). This was not nearly enough to meet its prior average annual operating loss of over $23,550 (G.X. 47; M. 3). The undisputed evidence further showed that in 1964 Citizen Publishing would have sustained a loss of more than $75,000 if it were restricted to an agreement providing only for joint use of printing and distribution facilities (D.X. 163).

The government makes much of the fact that Star Publishing and Citizen Publishing are now healthy and operating at a profit (M. 6). The profit, before taxes, of these appellants is approximately the same as that of the "average medium city newspaper," which in 1964 was 19.2 per cent of revenues (Editor & Publisher, Apr. 16, 1966, p. 11).

The issue here is not whether Star and Citizen are now making a profit, but whether both could survive in the Tucson market without the operating agreement. Significantly, Tucson is the only city in Arizona with two competing newspapers. The richer, larger Phoenix market has two newspapers, but they are owned by the same person. Failures in recent years include the Phoenix *Arizona Times* (1949), the Prescott *Courier-Journal* (1958), the Phoenix *Arizona Journal* (failed twice, 1963, 1964), and the Phoenix *Arizona Journal News* (1965).*

C. The Section 2 and Relief Issues.

The government argues that summary disposition of the Section 1 charge did not prejudice appellants' defense of the Section 2 issues and the question of relief (M. 17, fn. 14).

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*American Newspaper Publishers Association Bulletin No. 5203, July 27, 1950; Bulletin No. 5703, Feb. 6, 1959; General Bulletins Nos. 5 (Jan. 29, 1964), 5 (Feb. 3, 1965), and 6 (Feb. 9, 1966).

The motion to affirm shows that this is not so. The government points out that the District Court found that the relevant market comprised the publication of newspapers of general circulation to the exclusion of other mass media (M. 10-11; F. 60-181). The government also notes that the Court concluded that appellants had power over the circulation and advertising rates of their newspapers (M. 11). The government goes on to explain that the Court concluded that this power was derived directly from the 1940 operating agreement (C.L. 3, 4; M. 11). Having found that the 1940 agreement was illegal per se, it was inevitable that the Court would conclude that appellants had combined and conspired through that agreement to obtain power over circulation and advertising rates and thereby monopolize the newspaper market (M. 11). (See *United States v. Griffith* (1948) 334 U.S. 100, 106.) This was the very argument the government made below.*

Thus, the Court's summary disposition of the Section 1 charge had an extremely prejudicial effect upon appellants' Section 2 defense. When the operating agreement was summarily declared per se illegal, for all practical purposes appellants had lost the entire case. Consequently, the District Court granted the relief requested by the government.

D. The Importance of This Case.

The government tries to minimize the importance of the decision in this case by saying that the issues here do not affect the legality of "*all* joint operating agreements, or indeed, of all aspects of appellants' agreement" (M. 16).

The Memorandum of Amici Curiae in Support of Jurisdictional Statement advises that some 44 newspapers

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*Government's Memorandum in Opposition to Motion to Relieve Defendants of Application of Portion of Pre-Trial Order and to Reopen the Issues for Trial, pp. 1-2; Government's Post-Trial Brief, p. 24.

throughout the country are parties to operating agreements which, like the Tucson agreement, provide for the merger or consolidation of their mechanical, circulating and advertising functions (p. 2, fn. 2; p. 3, fn. 4). They state that if the judgment below is sustained, "virtually every city in which an operating arrangement exists inevitably will become either a one newspaper city or a city in which newspapers are published under single ownership" (p. 10).

These other joint operations have good cause for alarm because counsel for the government advised the District Court that "the decision in this case will be a large factor in judging what action is appropriate to take in other similar situations" (Tr. Feb. 13, 1967, p. 20). Further, the District Court was well aware from the outset that "'the Government views this case as a test case which will guide the Department's policy toward newspapers throughout the nation'" (Tr. Jan. 8, 1966, p. 30).

The government attempts to minimize the importance of this case by saying that "the price-fixing and profit-pooling provisions here involved do not constitute arrangements of first impression, but are practices which have long been familiar to the courts and have consistently been held unlawful *per se*" (M. 16). No case or other authority is cited to support that proposition. Before the notice of appeal was filed, the government advised the trial court precisely to the contrary.

> "MR. CONNELL: Your Honor, this is a different case from any case the Anti-Trust Division has yet brought in the newspaper field. That is a fact * * * this is the first time we have sued on this type agreement" (Tr. Feb. 13, 1967, p. 20).

In stating that the decree below does not abrogate the operating agreement (M. 11, fn. 7), the government overlooks the fact that the record without contradiction shows

that without the provisions for joint advertising and circulation departments and the distribution of revenues in established ratios, the operating agreement could not achieve its purpose and the Citizen will fail.*

E. The 1965 Acquisition.

The District Court did not give Small, Jr., the choice of disposing of either Star or Citizen—it ordered Small to dispose of Star. In our jurisdictional statement we advise that "[a]ppellants do not oppose the divestiture, but contend that the mode of divestiture should be modified" (J.S. 4, 8). By this we mean that the order should permit Small to sell either Star or Citizen, because if the judgment of the District Court is permitted to stand, and the operating agreement thereby rendered unworkable, Citizen will again become a failing company.†

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*The government points out that, in 1965, 23 cities smaller than Tucson had two or more competing daily newspapers not operating under a joint production plan (M. 23, fn. 18). This is not inconsistent with our statement that "[t]here is today no city in this country the size of Tucson which can or does support two *metropolitan* newspapers operating independently at both the commercial and journalistic levels; * * * newspapers in much larger cities throughout the country are failing and have been forced either to merge completely or to enter into operating agreements * * *" (J.S. 12) (emphasis added). Smaller towns occasionally have competing newspapers which are supported by job printing arrangements, subsidies from outside sources and affiliations with television stations (Tr. 858). The basic reason these newspapers are able to survive, however, is the vast difference in the cost of operating a small, localized paper, as compared with *metropolitan* dailies such as the Tucson papers (Tr. 756-758). Even so, since 1965 competing newspapers have suspended in two of the 23 smaller cities (Lima (Ohio) *Star* (6/22/66); Kokomo (Ind.) *Times* (11/7/67)) (American Newspaper Publishers Association General Bulletins, Nos. 7 (Feb. 8, 1967) and 10 (Feb. 21, 1968)).

†The District Court found that the fact that Star has a Sunday edition while the Citizen does not would give Star an advantage in competing with Citizen (F. 193). It also found that it is impossible to predict what the operating results of either newspaper will be in a competitive situation (F. 192). The evidence is uncontradicted, however, that if the operating agreement is dissolved, Citizen will immediately operate at a loss (D.X. 163).

Appellants urged the District Court to consider the change in status quo which would be wrought by its decree of divestiture (Tr. 51-54) and they pointed out that there was no reason why separation of the two newspapers should be made more difficult for appellants than necessary (citing *United States v. Pullman Co.* (E.D. Pa. 1944) 53 F.Supp. 908, 908-909, Post-Trial Brief for Defendants, p. 107)*.

CONCLUSION

The motion to affirm should be denied.

Respectfully submitted,

RICHARD J. MACLAURY
THOMAS J. KLITGAARD
Attorneys for Appellants

Of Counsel

JOHN L. DONAHUE, JR.
ROBERTSON & FICKETT
Tucson Federal Savings Tower
Tucson, Arizona 85702

GEORGE READ CARLOCK
RYLEY, CARLOCK & RALSTON
Title & Trust Building
Phoenix, Arizona 85003

PILLSBURY, MADISON & SUTRO
225 Bush Street
San Francisco, California 94104

Dated: October, 1968.

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*While appellants do not concede that the acquisition of Star violated Section 7 of the Clayton Act, as the government claims (M. 13, 24), they do not oppose divestiture if the operating agreement remains substantially intact. This is because the Smalls contemplated the prompt disposal of Star when it was acquired. They informed the Justice Department of this intent prior to the acquisition and before the complaint was filed (Tr. 2422).